No. 12019

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

HARRY C. WESTOVER, United States Collector of Internal Revenue, Sixth Collection District of California, and UNITED STATES OF AMERICA,

Appellants,

vs.

AGNES F. SMITH,

Appellee.

Appeal From the District Court of the United States for the Southern District of California,

---

BRIEF FOR THE APPELLANTS.

THERON LAMAR CAUDLE,
Assistant Attorney General.

ELLIS N. SLACK,
ROBERT N. ANDERSON,
HOMER R. MILLER,
Special Assistants to the Attorney General.

JAMES M. CARTER,
United States Attorney.

GEORGE M. BRYANT,
Assistant United States Attorney.

EDWARD H. MITCHELL,
Assistant United States Attorney.

Parker & Company, Law Printers, Los Angeles. Phone TR. 5206.

TOPICAL INDEX.

INDEX TO APPENDIX.

TABLE OF AUTHORITIES CITED.

Cases.

Statute.

Miscellaneous.

No. 12019

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

Harry C. Westover, United States Collector of Internal Revenue, Sixth Collection District of California, and United States of America,

Appellants,

vs.

Agnes F. Smith,

Appellee.

BRIEF FOR THE APPELLANTS.

Opinion Below.

The District Court wrote no opinion.

Jurisdiction.

This is an appeal from a judgment in favor of the taxpayer for the refund of income taxes for the years 1941 and 1943, in the amount of $38,115.62, plus interest. Within the time allowed by law a claim for refund for 1941 was filed with the Collector of Internal Revenue for the Tenth District of Ohio [R. 7], and a claim for 1943 was also filed within time with the appellant Collector [R. 10]. The Commissioner notified taxpayer by registered mail of the disallowance of these claims on June 11, 1947 [R. 8], and June 10, 1947 [R. 10], respectively.

This action was commenced in the District Court on August 11, 1947 [R. 28], within two years after the Commissioner's notice of disallowance of both claims, in conformity with the provisions of Section 3772(a)(2), Internal Revenue Code.

The taxes for 1941 were paid to the Ohio Collector who has been out of office since January 1, 1944 [R. 6-7]. The taxes for 1943 were in part paid to the Ohio Collector [R. 9], and in part to the appellant Collector, the latter being in office on the date of this suit [R. 11].

The District Court had jurisdiction under Section 24, Twentieth, of the Judicial Code even though the amount sued for exceeded $10,000. Taxpayer filed a motion for summary judgment [R. 35] which was sustained by the District Court [R. 46-47]. Judgment of the District Court was entered May 28, 1948 [R. 48-50]. Notice of appeal was fixed within sixty days thereafter on July 14, 1948 [R. 51]. This Court has jurisdiction under the provisions of 28 U. S. C., Section 1291.

Question Presented.

In 1940 Quickwork Company in its dissolution and liquidation transferred to taxpayer, its sole stockholder, in exchange for her stock in the corporation, all of its assets including assets of a determinable value and a contractual right to receive from the Whiting Corporation certain payments, the amount of which depended on certain gross sales thereafter made by Whiting. The fair market value of this right on the date of its receipt by taxpayer was not ascertainable though it was recognized to be of substantial value. The question presented is whether payments received by taxpayer from this right in subsequent

years, which were in excess of the adjusted basis of taxpayer's stock previously recovered, were taxable to her as ordinary income or constituted capital gains under Sections 115(c) and 117(a)(4), Internal Revenue Code.

Statute and Regulations Involved.

The pertinent statute and Regulations are set forth in the Appendix, *infra.*

Statement.

Taxpayer brought this action to recover income taxes for 1941 and 1943, in the sum of $37,107.96, plus interest [R. 2-11]. The answer admitted most of the material allegations of the complaint aside from legal conclusions [R. 29-32]. The taxpayer filed a motion for summary judgment based on the facts as admitted by the pleadings or as supported by an affidavit as to the allegations which were denied [R. 35-41]. The Court granted taxpayer's motion for a summary judgment and entered judgment accordingly [R. 46-50].

The undisputed facts pertinent to this controversy as admitted by the pleadings or as set out in taxpayer's affidavit may be briefly summarized as follows:

The Quickwork Company was an Ohio corporation engaged in the manufacture and sale of certain machine tools consisting principally of various types of rotary shears. It owned patents and drawings covering the manufacture of such machines and in addition to the manufacture and sale thereof had licensed other companies to manufacture similar machines on a royalty basis. In 1933, taxpayer acquired all of Quickwork's outstanding stock which she continued to own up to the date of the liquidation of the corporation in 1940 [R. 2-3].

On May 31, 1940, Quickwork entered into an agreement with Whiting Corporation for the sale to the latter of all of its assets, exclusive of cash and miscellaneous items. The agreement provided that Whiting should pay in consideration for the assets $15,000 in cash, certain fixed amounts of a minor nature and 10% of the gross sales price to Whiting on all machinery and equipment thereafter developed and manufactured by it as a result of acquiring the machinery, patents and patterns of Quickwork. The obligation to make these payments on a percentage basis was to continue in any event until May 31, 1950, and thereafter during the lifetime of taxpayer, who was 57 years of age on the date of the agreement [R. 3].

For many years the annual sales of Quickwork had been substantial and both parties realized that the impending war would be likely to increase considerably the demand for and sales of the Quickwork line [R. 36-37]. While the parties realized the agreement to pay the 10% based on gross sales had a substantial value, there was no way of ascertaining the measure of the value at the time of the sale "and said agreement then had no ascertainable fair market value" [R. 4].

Shortly after May 31, 1940, pursuant to the contract, Quickwork transferred and delivered by bill of sale to Whiting complete title to the assets described in the agreement and thereupon ceased to have any interest in such assets. Shortly thereafter, Quickwork decided to liquidate and dissolve. Under date of August 24, 1940, it transferred to taxpayer by a bill of sale and assignment all of its assets of whatsoever nature including its rights against Whiting under the agreement of May 31, 1940, in complete liquidation and cancellation of all of its outstanding stock which was then owned solely by taxpayer who surrendered her stock for cancellation and retirement, after

which it was cancelled and retired without later being reissued. In due course thereafter, Quickwork was dissolved [R. 4-5].

The adjusted basis of taxpayer's stock on the date of liquidation was $34,000. She received in final liquidation assets of the total value of $39,204.26, exclusive of the right to the percentage payments under the agreement between Quickwork and Whiting. At the time of its receipt by taxpayer, the contractual right had a very substantial value. However, there was no way of ascertaining the measure of the value and therefore it had no ascertainable fair market value. Because of this no value was assigned to it in determining the amount of taxpayer's capital gain upon said liquidation [R. 5].

In 1941, taxpayer received as percentage payments from Whiting under the contract $37,231.68, which she reported in her federal income tax return for that year as ordinary income and paid a tax thereon [R. 6]. In 1943, she received further percentage payments under the contract in the sum of $65,412.64, which she likewise reported as ordinary income and paid a tax thereon [R. 8]. Taxpayer alleges her treatment of these items as ordinary income was erroneous and that they represented capital gains realized by taxpayer on the exchange of her stock in Quickwork in complete liquidation of that company [R. 7, 9-10].

Statement of Point to Be Urged.

The District Court erred in sustaining taxpayer's motion for summary judgment and in finding and holding that the amounts received in 1941 and 1943, on the assigned contractual right, were amounts received in complete liquidation of Quickwork and that they should be treated as capital gains rather than ordinary income.

Summary of Argument.

The assets distributed to taxpayer under the complete liquidation of Quickwork are treated under Section 115(c), Internal Revenue Code, as being received in full exchange for her stock. These assets here consisted of money and property of fixed value plus a contractual right of substantial but unascertainable value.

The gain on the exchange (which is a capital gain under Section 117(a)(4), Internal Revenue Code) is measured under Section 111(a)(b) and Section 115(c), Internal Revenue Code, by the difference between the value of the money and property received and the adjusted basis of taxpayer's stock.

Taxpayer's capital gain on the transaction was realized in 1940, the money and the property being in excess of the adjusted basis of her stock without considering the contractual right. Since it was impossible to value the contractual right its value was correctly reported as zero and taxpayer realized capital gain to the extent of the value of the property received above the basis of the stock. The sums received in later years were not received in exchange for taxpayer's stock but were derived from the contractual obligation and not being received from the sale or exchange of capital assets they constituted ordinary income rather than capital gains.

The decision of the court below was therefore incorrect in treating the amounts received under the contract as being amounts distributed in complete liquidation and thus capital gains. They were ordinary income derived from the contract regardless of the value or lack of value of the contract when received.

ARGUMENT.

The Income Received From the Contracts in 1941 and 1943 Did Not Arise From the Sale or Exchange of Capital Assets and Therefore Constituted Ordinary Income and Not Capital Gains.

In August, 1940, taxpayer, the sole owner of the stock of Quickwork Company, received all of the assets of that company in complete liquidation in exchange for her stock. The adjusted basis of her stock was $34,000, and the cash and assets that could be valued at the time were worth $39,204.26. Besides these assets taxpayer received absolutely a contractual right under a contract entered into between Quickwork and the Whiting Corporation on May 31, 1940, whereby she became entitled to receive 10% of Whiting's gross sales prices less certain taxes and commissions on all machinery or equipment (with some exceptions) thereafter sold by Whiting and which were developed and manufactured by Whiting or upon its order as a result of the acquisition of various articles referred to in the contract [R. 16]. Both Whiting and Quickwork recognized the contractual right as having a substantial value [R. 4]. This was also recognized by taxpayer on the date of its distribution to her by Quickwork [R. 5]. However, there were no means of ascertaining its fair market value at that time and consequently in her income tax return for 1940, taxpayer assigned it no value in determining the capital gain on the liquidation and reported capital gain of only $5,204.26.

In 1941 and 1943, taxpayer received from Whiting payments pursuant to this contractual right in the respective amounts of $37,231.68 and $65,412.64 [R. 6, 8]. The controversy here is over whether these payments are ordinary income under Section 22(a), Internal Revenue Code

(Appendix, *infra*), and reportable in full or capital gains so that taxpayer may take into account only the percentages set forth in Section 117(b), Internal Revenue Code (Appendix, *infra*).

It is our position that the sums are not capital gains because taxpayer did not receive them as property distributed in liquidation of Quickwork in exchange for her stock and consequently they did not arise from the sale or exchange of capital assets. She did not receive the payments from or through Quickwork but from Whiting under the contractual right which had been previously received by taxpayer in liquidation of her corporation. Taxpayer here is not entitled to treat the payments as capital gains in 1941 and 1943, because they were not in fact capital gains from the *sale* or *exchange* of a capital asset as defined in Section 117(a)(1)(4), Internal Revenue Code (Appendix, *infra*), but were ordinary income arising from a contract. The contractual right had not been sold or exchanged. In considering this problem we mention briefly several legal principles involved which are well settled and not in serious dispute between the parties:

1. The term "capital gains" is expressly made to apply only to gains from the *sale* or *exchange* of capital assets. Section 117(a)(4); *Helvering v. Flaccus Leather Co.*, 313 U. S. 247; *Fairbanks v. United States*, 306 U. S. 436; *Kieselbach v. Commissioner*, 317 U. S. 399; *Hale v. Helvering*, 85 F. 2d 819 (App. D. C.). Where it does not arise from the sale or exchange of a capital asset gain must be reported as ordinary income. *Fairbanks v. United States, supra.*

2. Under Section 115(c), Internal Revenue Code (Appendix, *infra*), taxpayer is entitled to treat a distribution in complete liquidation as property received in full ex-

change for her stock, and is entitled to apply the capital gains provisions in determining gain or loss on her stock on the theory there has been an exchange of her stock for assets. *Helvering v. Weaver Co.,* 305 U. S. 293; *White v. United States,* 305 U. S. 281.

3. Under Section 115(c), gain on a complete liquidation is determined under Section 111, Internal Revenue Code (Appendix, *infra*), and recognized to the extent provided under Section 112, Internal Revenue Code (Appendix, *infra*). It is conceded that none of the exceptions in Section 112 are here applicable so that the entire gain must be recognized subject to Section 117(b). Under Section 111 (a) and (b), Internal Revenue Code (Appendix, *infra*), the amount of gain realized is the sum of money received plus the fair market value of *property* other than money received, less the adjusted basis of the stock. It is not disputed that the sums received were in excess of the basis of the stock and constituted taxable income.

The problem here seems to hinge on whether the payments involved were in fact property or money received as a distribution in exchange for taxpayer's stock as defined in Section 111(b), or were derived from property so received.

The lower court held that the payments of $37,231.68 and $65,412.64 were amounts received in exchange for the stock. In reaching its decision the court relied strongly on *Carter v. Commissioner,* 9 T. C. 364, (pending on appeal in the Court of Appeals for Second Circuit).[1] The facts in that case are so similar to those here involved that the cases are probably indistinguishable. However, we

---

[1]That case has been argued on appeal but was undecided at the time of writing this brief.

contend that the decision is incorrect and that the Tax Court erred in its view that the decision in *Burnet v. Logan*, 283 U. S. 404, required that the payments there involved must be treated as part payment in exchange for the stock.

In the *Logan* case, *supra*, the taxpayer *sold* her stock for cash plus a contractual right given her by the purchaser to receive unascertainable amounts payable annually based on future production of iron ore. The Court held that the future royalties did not constitute taxable income in the years actually received because taxpayer had not yet recovered her capital investment in the stock and in determining whether the basis had been recovered refused to value the contractual right because of its speculative value. The Court took the position that this sale was not a closed transaction in the year title to the stock passed because of the contingent payments to be received in the future.

Some of the distinguishing features between that case and the case at bar are:

1. The transaction there involved was a sale rather than an exchange as here involved. This was emphasized by the Court in its opinion (p. 412).

2. In the case at bar taxpayer had recovered the basis of her stock in 1940 prior to the tax years involved while there the basis had not been recovered in the tax years and it was held no taxable income arose until such recovery took place.

3. There the future payments were due and owing from the purchaser under a promisor-promisee relationship. Here there is no such relationship, taxpayer having received the right in exchange for her stock, which right was clearly a property right enforceable against another

company effective from the date of its assignment and one which taxpayer could enforce without reference to Quickwork.

4. In the *Logan* case, *supra,* there were grounds for considering the transaction still open, which grounds do not exist in the instant litigation. The purchaser there was required to make contingent payments over future periods pursuant to the contract. Here, Quickwork Company, in exchange for an absolute transfer of the stock, assigned unconditionally all of its assets including the contractual right and immediately thereafter dissolved. It had no further interest or connection with the contractual right and as between Quickwork and taxpayer the transaction was fully and completely closed.

5. The *Logan* case did not involve the provisions of Section 117 (a) and (b), Internal Revenue Code, or similar provisions of Revenue Acts. The Court there did not construe the capital gains provisions of the statutes, and its holding is not inconsistent with treating the contractual right as property under Section 111(b). It was not a question there of whether the sums involved were capital gains or ordinary income, but the question was whether they constituted taxable income at all. The Court held they did not because the capital investment had not been recovered.

We submit that the *Logan* case is readily distinguishable from the case at bar. There is nothing in the Court's opinion to suggest that the income here realized in later years should be related back to the sale or exchange and valued at its face amount in determining the gain. Section 111(b) clearly requires that the property shall be valued according to its fair market value when received. Further, Section 115(c) treats amounts distributed in complete

liquidation of a corporation as being in full payment in exchange for the stock.[2]

Taxpayer argues in effect that since the value of the contract could not be ascertained, she is entitled to treat the payments as in lieu of the "amount realized" as defined in Section 111(b). She contends that the payments may be treated as capital gains in 1941 and 1943, whereas the gain from her exchange of stock is clearly under the applicable law recognizable on the date the transaction was completed, that is when the exchange was fully carried out which we submit was in 1940. We believe there is no warrant here for extending the provisions of the statutes beyond the clear import of the language used. *Gould v. Gould,* 245 U. S. 151; *United States v. Merriam,* 263 U. S. 179. The exchange here was complete in 1940, and any gain on the stock was realized in that year.

In the *Logan* case, *supra,* the Court stated (p. 412), "The 1916 transaction was a sale of stock—not an exchange of property." This statement indicates that a different conclusion might have been reached if there had been an exchange of stock under a complete liquidation of a corporation, the corporation distributing all of its assets including a contract to that taxpayer as was the situation here. We have shown that the Court there did not construe Section 111(b), Internal Revenue Code, or

---

[2]It has been stated that the doctrine of the *Logan* case should be applied sparingly in order to accelerate the taxation of income rather than defer recognition of taxable gains. 1 Mertens, Law of Federal Income Taxation, Sec. 5.07. See for example, *Brown v. Commissioners,* 26 B. T. A. 781, affirmed, 69 F. 2d 863 (C. C. A. 5th), certiorari denied, 293 U. S. 579, holding that where a taxpayer entered into a contract for the cutting of timber owned by her she was not entitled to recover her full investment on the value of the entire timber contract before reporting her liability for income tax on the profits derived from the timber cut and sold.

similar provisions of Revenue Acts providing that in determining gain in a sale or other disposition of property except an installment sale under Section 111(d), the amount realized shall be the sum of money received "plus the fair market value of the property (other than money) received." We therefore submit that the *Logan* case is not authority supporting taxpayer's position.

It is clear that the contractual right here involved constituted "property" received by the taxpayer under the provisions of Section 111(b). The term when as here used broadly in the statute clearly includes obligations, rights and other intangibles as well as physical property. *Citizens State Bank of Barstow, Tex., v. Vidal,* 114 F. 2d 380 (C. C. A. 10th). The term "property" when so used extends to everything of value including easements, franchises, improvements and incorporeal hereditaments. *Hoyd v. Citizens Bank of Albany Co.,* 89 F. 2d 105 (C. C. A. 6th). It has been stated that the term "property" includes anything which has an exchangeable value or goods to make up a man's worth including any interest or estate which the law recognizes as of sufficient value for judicial recognition. *Samet v. Farmers' & Merchants' Nat. Bank,* 247 Fed. 669 (C. C. A. 4th). It is well settled that it covers intangibles as well as tangibles. *Levy v. Commissioner,* 131 F. 2d 544 (C. C. A. 2d); *Tri-Lakes S. S. Co. v. Commissioner,* 146 F. 2d 970 (C. C. A. 6th); *City and County of San Francisco v. United States,* 106 F. 2d 569 (C. C. A. 9th).

It is clear that the taxpayer here received as "property" under Section 111(b), a contractual right which she did not sell or exchange, but continued to hold receiving payments therefrom which did not arise from

a sale or exchange of such right but as income from the investment. Such payments were ordinary income rather than capital gains. (*Puelicher v. Commissioner,* 6 T. C. 300; *Kieselbach v. Commissioner,* 317 U. S. 399.)

The principles above stated are well illustrated by the *Kieselbach* case, *supra.* There the City of New York obtained title to that taxpayer's property under a condemnation proceeding. Several years later the Supreme Court of New York entered a decree fixing the value of the property under which the taxpayer was entitled to receive its fair market value on the date of condemnation plus interest from that date. The title to the property vested in the City of New York on the date of the condemnation but payment was not received until after the decree. The Court held that the principal sum represented proceeds from an involuntary sale of capital assets and should be treated as capital gains in so far as they exceeded the adjusted basis of the property. However, it held that the interest which was paid after title to the property had passed to the city constituted ordinary income as not being part of the sales price. Although it was argued that in common acceptation the interest received was in payment of the property sold, the Court refused to so construe it and held rather that it was a sum derived from a right which had already been acquired on account of the delay in payment which could not be treated as proceeds from the sale of a capital asset. Here, as there, the payments arose from a right which had already been acquired and not pursuant to a

sale or exchange.[3] It would apparently be conceded here that if the right could have been valued in any given amount when received, it would have been includible in reporting capital gain in 1940 and in that case no question would have arisen as to the payments being ordinary income. It is obvious that the fact that the right had no ascertainable fair market value at the date of acquisition cannot alter the provisions of the statute with respect to the computation of the capital gains from the exchange in that year. The only effect the value or lack of value of the property received has upon the computation of the capital gains is with respect to determining the size or extent of such gains at the time of the exchange.

Income is determinable as at the close of a tax year without regard to subsequent events not then predictable or foreseeable. (*Penn v. Robertson,* 115 F. 2d 167, 175 (C. C. A. 4th); *Moore v. Thomas,* 131 F. 2d 611 (C. C. A. 5th).) A taxpayer may not postpone the payment of taxes in order to ascertain the final outcome of the transaction out of which there arose a gain or loss. (*Blum v. Helvering,* 74 F. 2d 482 (App. D. C.).) As the court stated in *Boudreau v. Commissioner,* 134 F. 2d 360, 361 (C. C. A. 5th):

> "Under the express provisions of the applicable statutes, when there is complete liquidation of a corporation, stockholders are accountable for the

---

[3]See also *Esperson v. Commissioner,* 127 F. 2d 370 (C. C. A. 5th), holding that where a taxpayer under a conveyance of oil interests reserved an interest in the oil in place that the "in-oil" payments did not constitute capital gain from the sale of capital assets but were receipts from income producing operations. See also *Fleming v. Commissioner,* 153 F. 2d 361, 363 (C. C. A. 5th); *Boudreau v. Commissioner,* 134 F. 2d 360 (C. C. A. 5th).

difference between the cost basis of their stock and the fair market value of the property received in exchange for it."

And in *Fleming v. Commissioner,* 153 F. 2d 361, 363 (C. C. A. 5th), the court stated—"The exchange is an income-realizing event, and the fair market value of the distributed assets must be determined." There is nothing in the statutes or in the rationale in the case of *Burnet v. Logan,* 283 U. S. 404, which would permit the payments here in question to be treated as received under an exchange merely because the right from which they were derived was not susceptible of valuation at the time of its acquisition. If property received on an exchange had no fair market value then no taxable gain or deductible loss was realized. (*Mount v. Commissioner,* 48 F. 2d 550 (C. C. A. 2d); *Tsivoglou v. United States,* 27 F. 2d 564 (Mass.), affirmed, 31 F. 2d 706 (C. C. A. 1st).) It would follow that if part of the property only can be valued the gain is measured only by the value of that portion. The value or lack of value of the right certainly could not determine whether such right was received under an exchange.

The other cases relied upon by the Tax Court in *Carter v. Commissioner,* 9 T. C. 364, are readily distinguishable on their facts. In the cases of *Haynes v. United States,* 50 F. Supp. 238 (C. Cls.); *Nicholson v. Commissioner,* 3 T. C. 596; *Imperial Type Metal Co. v. Commissioner,* 106 F. 2d 302 (C. C. A. 3d); and *Commissioner v. Hopkinson,* 126 F. 2d 406 (C. C. A. 2d), the property involved was sold on the installment plan with the pur-

chase price to be discharged by future payments. It was held that payments of the purchase price collected in the future tax years were capital gains because they constituted gain from the sale or exchange of a capital asset. But the payments collected by the taxpayer here were, as we have already emphasized, not the result of a sale or exchange of a capital asset, but merely the collection of income stemming from property received on the exchange and were not even collected from a party to the exchange.

Taxpayer's position here is analogous to an argument that if the corporation's assets distributed to taxpayer had included bonds or real estate the interest and rent later collected should be related back to the exchange and treated as capital gains in years subsequent to the exchange. This is patently erroneous and as we have shown is contrary to Section 115(c), and in addition inconsistent with the purposes underlying the capital gain statutory scheme outlined by the court in the *Hopkinson* case *supra* (p. 410).[4] The *Logan* case *supra,* certainly does not require such treatment.

Finally we emphasize there is clearly no authority under the statutes for a deferment plainly inconsistent with the statutes in the recognition of a capital gain from an exchange such as here where title to the capital

---

[4]As the court points out there, the enactment of statutes providing for the treatment of capital gains was a measure to furnish relief from high surtaxes occasioned by the enhancement in value of property over a number of years.

stock and assets exchanged therefor fully passed, until a later year when the full amount of the income to be derived from a contractual right received on such exchange had been recovered. Such a treatment would be inconsistent with the policy of the law which is designed to accellerate and not delay the reporting of income. It is, of course, proper to value the contract if that is possible. It is only in rare cases that such impossibility exists. (*Boudreau v. Commissioner,* 134 F. 2d 360, 361 (C. C. A. 5th).) The inability to value the contract favors the taxpayer in reducing his capital gain, but at the same time creates the disadvantage of a low basis for gain or loss on the property received if sold or exchanged in the future. Certainly the basis of the contract would be zero under a sale or exchange under the facts as admitted here. All this could have no possible effect on the treatment of the income from the contract any more than it could have on the treatment of rent, interest or dividends received on other property received under any sale or exchange.

In view of the foregoing there is no authority for taxpayer's valuing the contracts on the basis of the subsequent payments. The transaction was complete when titled passed in August, 1940. (*Cf. Bedell v. Commissioner,* 30 F. 2d 622, 624 (C. C. A. 2d); *Commissioner v. Union Pac. R. Co.,* 86 F. 2d 637 (C. C. A. 2d).) The subsequent payments were not proceeds of a sale or exchange but income taxable under Section 22(a) and not capital gains.

Conclusion.

The judgment should be reversed.

Respectfully submitted,

THERON LAMAR CAUDLE,
Assistant Attorney General.

ELLIS N. SLACK,
ROBERT N. ANDERSON,
HOMER R. MILLER,
Special Assistants to the Attorney General.

JAMES M. CARTER,
United States Attorney.

EDWARD H. MITCHELL,
Assistant United States Attorney.

GEORGE M. BRYANT,
Assistant United States Attorney.

November, 1948.

APPENDIX.

Internal Revenue Code:

SEC. 22. GROSS INCOME.

(a) GENERAL DEFINITION.—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * * (26 U. S. C. 946 ed., Sec. 22.)

* * * * * * * * *

SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

(a) COMPUTATION OF GAIN OR LOSS.—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113(b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

(b) AMOUNT REALIZED.—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

(c) RECOGNITION OF GAIN OR LOSS.—In the case of a sale or exchange, the extent to which the gain

or loss determined under this section shall be recognized for the purposes of this chapter, shall be determined under the provisions of section 112.

(d) INSTALLMENT SALES.—Nothing in this section shall be construed to prevent (in the case of property sold under contract providing for payment in installments) the taxation of that portion of any installment payment representing gain or profit in the year in which such payment is received. (26 U. S. C. 1946 ed., Sec. 111.)

* * * * * * * * *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) GENERAL RULE.—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section. (26 U. S. C. 1946 ed., Sec. 112.)

* * * * * * * * *

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

(c) DISTRIBUTIONS IN LIQUIDATION.—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. * * * (26 U. S. C. 1946 ed., Sec. 115.)

* * * * * * * * *

Sec. 117. Capital Gains and Losses.

(a) Definitions.—As used in this chapter—

(1) Capital Assets.—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of which taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(1);

* * * * * * * * *

(4) Long-term Capital Gain.—The term "long-term capital gain" means gain from the sale or exchange of a capital asset held for more than 18 months,[5] if and to the extent such gain is taken into account in computing net income;

* * * * * * * * *

(b) Percentage Taken into Account.—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net capital gain, net capital loss, and net income:

* * * * * * * * *

(26 U. S. C. 1946 ed., Sec. 117.)

---

[5]Section 150, Revenue Act of 1942, c. 619, 56 Stat. 798, changed this to "6 months."

Treasury Regulations 103, promulgated under the Internal Revenue Code:[6]

SEC. 19.111-1. *Computation of Gain or Loss.*—Except as otherwise provided, the Internal Revenue Code regards as income or as loss sustained, the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent. The amount realized from a sale or other disposition of property is the sum of any money received plus the fair market value of any property which is received. The fair market value of property is a question of fact, but only in rare and extraordinary cases will property be considered to have no fair market value. * * *

* * * * * * * * *

SEC. 19.115.5. Distribution in liquidation.—(a) *General.*—Amounts distributed in complete liquidation of a corporation are to be treated as in full payment in exchange for the stock and the amounts distributed in partial liquidation are to be treated as in part or full payment in exchange for the stock so canceled or redeemed. The gain or loss to a shareholder from a distribution in liquidation is to be determined, as provided in section 111 and section 29.111-1, by comparing the amount of the distribution with the cost or other basis of the stock provided in section 113; but the gain or loss will be recognized only to the extent provided in section 112.

---

[6]Similar provisions appear in the corresponding Treasury Regulations 111, promulgated under the Internal Revenue Code, Sections 29.111-1 and 29.115-5 governing the year 1943.